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In the Supreme Court of the United States

OCTOBER TERM, 1963

No. 46

PEOPLE OF THE STATE OF CALIFORNIA AND PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA,
Petitioners,

vs.

LO-VACA GATHERING COMPANY, HOUSTON PIPE LINE COMPANY, AND EL PASO NATURAL GAS COMPANY,
Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

Reply Memorandum for the People of the State of California and the Public Utilities Commission of the State of California

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In the Supreme Court of the United States

OCTOBER TERM, 1963

No. 914

PEOPLE OF THE STATE OF CALIFORNIA AND PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA,

Petitioners,

vs.

LO-VACA GATHERING COMPANY, HOUSTON PIPE LINE COMPANY, AND EL PASO NATURAL GAS COMPANY,

Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

Reply Memorandum for the People of the State of California and the Public Utilities Commission of the State of California

In accordance with Rule 24(4) of the Revised Rules of the Supreme Court of the United States, the Petitioners, the People of the State of California and the Public Utilities Commission of the State of California (California), submit this memorandum in reply to the joint brief filed by Lo-Vaca Gathering Company (Lo-Vaca), Houston Pipe

Line Company (Houston), and El Paso Natural Gas Company (El Paso), Respondents, in opposition to the petitions for a writ of certiorari to the United States Court of Appeals for the Fifth Circuit filed by California (No. 914), by Southern California Gas Company and Southern Counties Gas Company of California (Southern California Companies) (No. 915), and by the Federal Power Commission (Commission) (No. 990).

1. In its petition (p. 13) California pointed out that the decision of the court below creates an attractive gap in the comprehensive scheme of effective regulation over the transportation, production, and sale of natural gas. *Panhandle Eastern Pipeline Co. v. Public Service Commission*, 332 U.S. 507, 520 (1947); *Federal Power Commission v. Transcontinental Gas Pipe Line Corp.*, 365 U.S. 1, 28 (1961). By narrowly interpreting Section 1(b) of the Natural Gas Act the decision of the Court of Appeals in this case has exempted the sales of natural gas to be made by La Vaca and Houston pursuant to so-called "restricted-use" contracts from the Commission's regulatory jurisdiction over sales for resale in interstate commerce. A serious regulatory gap is created because, in the absence of federal regulation over these sales, the State of Texas, where the gas is produced, gathered, and sold to the interstate pipeline, cannot realistically be expected to regulate such sales for the protection of gas consumers in California, Arizona and New Mexico. Moreover, it is beyond dispute that California, Arizona and New Mexico are without authority to regulate these Texas sales.

Respondents nevertheless suggest that no regulatory gap exists because it is claimed that Texas has the power to regulate the La Vaca and Houston "restricted-use" sales and

is interested in the regulation of transactions within its jurisdiction (Br. in Op., pp. 16-23). Irrespective of Texas' power to regulate, respondents are careful not to assert that Texas will, in fact, exercise whatever jurisdiction it may possess for the protection of California natural gas consumers. On the contrary, reference is made by respondents to regulation by Texas of natural gas sales where the interest of that state in protecting its consumers is manifest, i.e., city gate sales and industrial sales of local concern (Br. in Op., pp. 21-22).

California has not and does not now assert that Texas has no interest in regulating sales of natural gas where such gas is consumed in Texas and paid for by Texas consumers. What California does assert is that Texas has no conceivable interest in regulating sales of natural gas the cost of which is to be borne by California consumers. And this observation is made only for the purpose of pointing out that federal regulation of these sales is required in order to preserve the comprehensive system of *effective* regulation which this Court has consistently held is the purpose of the Natural Gas Act. *Federal Power Commission v. Transcontinental Gas Pipe Line Corp., supra.* By denying to the Commission regulatory jurisdiction over the Lo-Vaca and Houston "restricted-use" sales the decision of the court below creates a gap in effective regulation and presents an important jurisdiction question which this Court should review.

At page 22 of their brief in opposition, respondents state:

> "In this regard, also, it should be noted that the concern of California and S. Cal. Gas that gas sold for resale at the California border will be unregulated is groundless. The Commission will continue to regulate El Paso's sales for resale at the California border. And, pursuant to standard regulatory procedure used to allocate jurisdictional and nonjurisdictional costs,

> the gas resold at the California border will be attributed to gas purchased by El Paso under jurisdictional sales, not Lo-Vaca and Houston restricted-use sales."

California does not claim that the Commission as a result of the decision below will be deprived of regulatory jurisdiction over gas sold for resale at the California border. The rates at which gas is sold for resale by El Paso to the California public utility gas distribution corporations, the Southern California Companies and Pacific Gas and Electric Company, under familiar cost of service ratemaking principles include all the costs incurred by El Paso in providing its service, including not only the cost of the gas delivered but all associated costs such as the cost of compressor fuel utilized by El Paso in transporting gas from Texas to California. In the quoted paragraph, respondents apparently overlook the fact that whether El Paso labels its gas as "fuel" or as "purchased gas", the cost incurred must ultimately be borne by California ratepayers.[1] It is therefore no comfort to California that "gas resold at the California border will be attributed to gas purchased by El Paso under jurisdictional sales, not Lo-Vaca and Houston restricted-use sales."

On the contrary, the distinction that respondents here attempt to draw goes far to reveal the so-called "restricted-use" contracts as artificial devices to avoid effective regulation at the very point where it can most efficiently be undertaken for the protection of natural gas consumers, that is,

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1. Respondents emphasize that the Lo-Vaca and Houston "restricted-use" sales are not only supported by contractual identification but will be separately identifiable through installation of meters, which will facilitate the bookkeeping involved (Br. in Op., p. 4). Presumably California gas consumers may be required through rates to defray over a period of time the cost of these metering facilities as well as the high cost of the gas to be earmarked for fuel purposes.

at the point where the sale is made to the interstate pipeline.

2. The "separability test" used by respondents as a template for their carefully tailored "restricted-use" contracts and relied upon by the Court of Appeals in holding that the Commission is without jurisdiction to regulate these sales should not be applied to defeat effective regulation and to create a gap in the comprehensive scheme of regulation envisioned by Congress when it enacted the Natural Gas Act. The "separability test" has its origin in this Court's opinion in *United States v. Public Utilities Commission of California*, 345 U.S. 295, 317 (1953), where the facts of that case precluded its application, and, more importantly, where there existed no danger of the creation of a regulatory gap. Moreover, there was no question of the creation of a regulatory gap in either of the two cases relied upon by the court below where the test was in fact applied: *City of Hastings v. Federal Power Commission*, 221 F.2d 31 (D.C. Cir. 1954), cert. denied 349 U.S. 920 (1955), and *North Dakota v. Federal Power Commission*, 247 F.2d 173 (8th Cir. 1957). Neither of these cases, in denying federal regulatory jurisdiction, deprived the gas consumers concerned of effective regulation, for such consumers could be effectively protected by the state regulatory agencies in question.

In the instant case, however, the application of the "separability test" defeats the purpose of the Natural Gas Act which was enacted to protect natural gas consumers from exploitation at the hands of private natural gas companies. *Federal Power Commission v. Hope Natural Gas Company*, 320 U.S. 591, 611 (1944). California insists that the regulatory consequences of the "restricted-use" contracts entered into by Lo-Vaca and Houston and El Paso should not, and

cannot be ignored. It should be recognized that the "separability test" was evolved in cases involving a question of distribution of regulatory jurisdiction between the federal government and the states and should not be utilized in this case to sustain an artificial arrangement designed by the parties to eliminate the possibility of effective regulation.

* * * * * * *

California views this case as containing important legal issues having significant national regulatory and economic impact. For the reasons stated herein, as well as for the reasons contained in California's petition for a writ of certiorari, California respectfully submits that the question here presented fully deserves review by this Court, and California prays that its petition for writ of certiorari be granted.

Respectfully submitted,

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